



August 28, 2015

Mr. Gerard Poliquin
Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, Virginia 22314-3428

Email: regcomments@ncua.gov

RE: NCUA's Member Business Loans and Commercial Lending Proposal, RIN 3133-AE37

Dear Secretary Poliquin and Members of the NCUA Board:

On behalf of the Board of Directors and Executive Management Team of Black Hills Federal Credit Union (BHFCU), I am writing in response to NCUA's request for comment on the proposed rule regarding Member Business Loans and Commercial Lending. Black Hills Federal Credit Union is a community chartered, low income designated credit union serving members in the South Dakota counties of Pennington, Meade, Fall River, Custer, Lawrence, Haakon, Hughes, Stanley, Butte, Dewey, Ziebach, Sully, Hyde, Buffalo, Jerauld, Sanborn, Miner, McCook, Turner, and Lincoln. Within our counties, we also serve the Cheyenne River Indian Reservation and a portion of the Crow Creek Indian Reservation in South Dakota. BHFCU currently serves 61,489 members and has assets of approximately \$1.050 billion.

We would like to thank the NCUA for listening to credit unions and taking steps to reduce the regulatory burden on credit unions who offer Member Business Loans (MBL). For example, we are pleased with the proposed changes to remove the unsecured lending cap, loan-to-value limits, the requirement for personal guarantees, and the proposed change to the MBL cap calculation. These changes give us more flexibility, which may allow us to approve more loans when prudent to do so. In addition, we thank you for clarifying that non-member business participation loans continue to be excluded from the MBL definition.

While we appreciate NCUA's efforts to provide more flexibility with the proposed rules, we believe the proposal needs some additions, significant adjustments, and clarification.

Board of Directors and Management Responsibilities

The proposed policy requires that the credit union's commercial loan policy address commercial lending practices, procedures, and organizational structure. Under the proposed MBL rules, we are required to have an excessive amount of detail in policy. This is overly burdensome and requires that our Board become heavily involved in the day to day management of the credit union's business lending program. This is not their role!

While we agree with the need to have well-defined MBL policies, we are strongly against policy being required to contain significant detail that is very procedural in nature. Requiring significant detail in policy does not allow us to have the flexibility we need to serve members, make timely decisions, and would be costly due to additional staff time required for tracking and reporting.

We concur with the requirement for the Board to approve and understand our commercial and MBL loan programs and the risk involved. As stated above, the proposed rules would put a heavy burden on our volunteers. We believe providing the Board with insignificant details will be counter-productive and take their focus off of the larger items that may pose a real risk to BHFCU. Many of the items listed in the proposed rule should be in procedures, not policy, and should be managed by the Business Loan Manager, the Chief Lending Officer, and the CEO, not the Board.

We suggest that almost all of the items in the proposed rule where it is stated that it must be in our commercial loan policy, be changed to state procedure. The proposed rule could give a bullet item list, detailing what must be in our operating procedures. Having these items in procedure, gives us the flexibility to react to members' needs, instead of going back to the Board with every minor change.

Principles Based vs Prescriptive

The NCUA is proposing a less prescriptive MBL/Commercial rule. While this is true in some instances, the proposed rule is still prescribing an incredible volume of detailed requirements in policy. This is very prescriptive!

As stated above, we appreciate the effort NCUA has made to amend the MBL rule to provide credit unions with greater flexibility and individual autonomy. Unfortunately, we believe the proposed rule will negatively impact many credit unions and be more burdensome to comply with than the current rules. Because of the increased tracking and reporting requirements, extensive updates to policy, etc., we believe we will need to increase staffing to comply with the proposed rule. In addition, the proposed rule will require our Board to be more involved in the day to day operation of the credit union and that is not their role.

Several specific items that we do not believe should be in policy are outlined below.

Loan Approval Process

The proposal specifies that the credit union's commercial loan policy must establish lending authority for approving credit decisions. In discussing this with examiners during a recent exam, it appears our Board would have to approve individual lending authorities and changes to these authorities. We don't believe this is at all necessary and is just one of many examples where the proposed rule will give us less flexibility to manage our own programs instead of more. Because our Board isn't involved in the day to day operation of the credit union, they have little knowledge of the qualifications of individual lenders. For this reason, they have given the CEO the authority to set individual lending limits.

Underwriting Standards

The proposal requires that policy must address the required analysis and depth of the financial review performed to support the credit decision. It further states that policy should establish the approval process, including lending authorities and the documentation of the credit decision, while outlining the required components of the credit approval document. It is also stated that policy must establish due diligence requirements to evaluate other sources of income or losses affecting the guarantors or principals to determine the global financial condition and the debt service ability of the borrower.

It appears the proposal requires us to establish, in policy, a threshold for the required financial reporting and establish requirements for financial projections of the borrower. In addition, the proposed rule states that policy should also set requirements for the financial reporting to support the credit decision and address the minimum criteria for historic reporting at the inception of the loan, as well as regular reporting after the loan is closed, and the required quality of financial information to establish an accurate and reliable assessment of financial trends. This section of the proposed rule goes on at length about the quality of the financial data that is to be obtained, including when audited financials may be required. In interpreting the proposed rule, we believe we would be required to put this information in our MBL policy.

While we agree that much of this information is needed when underwriting an MBL, we are adamantly against this being a requirement in policy as it is very procedural in nature.

Risk Management System

The proposed rule requires the credit union to establish policies and procedures to identify and manage risk at the inception of the loan and throughout the life of the loan. Under the proposed rule, our policy will need to address the following:

- Loan Covenants – Our policy should establish the requirements for the use of financial covenants, financial reporting, and regular site visits.
- Periodic Review – Our policy must set forth the requirements for periodic loan relationship reviews.
- Credit Risk Rating System – The proposed rule requires the credit union to incorporate a credit risk rating system to analyze and describe the credit risk of each loan.

We agree that most of the items listed above are important in operating a safe and sound business loan program; however, these are very procedural in nature and should not be in policy.

Loan Exceptions

The proposed rule states that our commercial loan policy may allow for exceptions to policy. It further states that policy must establish the process for approval and documentation of exceptions. The proposal requires that all exceptions to the loan policy need to be tracked and periodically reported to senior management and the Board.

We believe our Board should be allowed to grant certain positions the authority to make exceptions or waive requirements as appropriate. These items are not considered policy

exceptions, as they are within an individual's authority as approved by the Board. We further believe that our Board should be able to decide what items are considered an exception and how/when they are to be reported. We believe it is necessary for the Board to be aware of larger exceptions and those that create significant risk to the credit union. However, we believe it is unreasonable to have procedural details in loan policy and excessive oversight to have all exceptions to these policies be reported to the Board and Executive Management. To truly allow credit unions to manage their commercial and MBL programs, we need the ability to let our Board decide what types of exceptions they would like to review and how much detail they would like to have in policy. We don't believe this should be mandated by NCUA.

Collateral

The proposal requires that the credit union must establish a policy for monitoring collateral, including systems and processes to respond to changes in asset values. This is just one more area where our policies will become too detailed under the new proposed rules.

Construction and Development Loans

The proposed rule states that a credit union that elects to make construction or development loans must ensure that its commercial loan policy includes adequate provisions by which the collateral value associated with the project is properly determined and established. For a construction or development loan, collateral value is the lesser of the project's cost to complete, or its prospective market value. This portion of the proposed rule goes on for at least two pages describing collateral value. It appears all of this needs to be in policy.

The proposed rule also requires that a credit union's commercial loan policy meets the following conditions:

1. Qualified personnel representing the interests of the federally insured credit union must conduct a review and approval of any line item construction budget prior to closing the loan;
2. A credit union approved requisition and loan disbursement process is established;
3. Release or disbursement of loan funds occurs only after on-site inspections, documented in a written report by qualified personnel representing the interests of the credit union, certifying that the work requisitioned for payment has been satisfactorily completed, and the remaining funds available to be disbursed from the loan is sufficient to complete the project; and
4. Each loan disbursement is subject to confirmation that no intervening liens have been filed.

How exactly is this principles-based when NCUA is requiring massive amounts of detail to be in policy? This is another area where the proposed rule requires that we have pages of procedural information in our policy.

Associated Member/Borrower Definition

The proposed rule replaces the current rule's definition of "associated member" with the term "associated borrower," and updates the definition to be more consistent with the combination rules applicable to banks. The proposed definition introduces the concepts of direct benefit, common enterprise, and control. This is very confusing! Having multiple definitions to

consider makes it more difficult for credit unions to serve members and comply with regulations. It also complicates tracking, and is even more restrictive than the current regulation. We ask that you clarify the definition of “associated borrower” and eliminate the proposed definitions for direct benefit, common enterprise, and control.

Commercial vs Member Business Loan

The methodology for creating a category for “commercial” loans makes sense and may be necessary for safety and soundness purposes; however, this will make tracking and reporting on the 5300 Call Report even more complex and will be very time consuming. Overall, we are in favor of differentiating commercial loans from MBLs and understand this may be necessary in order to track non-member participation loans and other commercial loans. At a minimum, we ask that NCUA look for ways to lessen the reporting requirements on the 5300 Call Report by requiring less data or broader reporting categories to streamline the process.

Single Borrower or Group of Associated Borrowers

The proposed rule is essentially the same as the existing rule in regards to the single borrower and associated borrower limits. This rule sets the single borrower maximum loan limit to an aggregate of 15 percent of the credit union’s net worth. The proposed rule will allow credit unions to exceed the general limitation by 10 percent of the credit union’s net worth, if the amount above the 15 percent is secured by readily marketable collateral. This change is a slight improvement to the existing regulation; however, it will be of little help to most credit unions.

We are asking that NCUA consider a change to this section of the proposed regulation by increasing the single borrower limit from 15 percent of the credit union’s net worth to 25 percent of the credit union’s net worth.

Another option would be to change the calculation to allow a credit union to only consider the percentage of the specific owner’s ownership in the single borrower calculation. For example, if a guarantor is a 25% owner in a business that has a loan for \$10 million with the credit union, and they are a 25% owner of a different business with a loan for \$7 million with the credit union, we would not be required to consider the entire \$17 million against their aggregate borrower limit. Instead, we would consider \$4,250,000 towards their single borrower limit. In this scenario, the two business entities would need to be separate entities and the credit union would need to assess the risk and adequately document this exception.

In addition, we understand that the proposed rule eliminates all waivers. If the two suggestions listed above are not an option, then we would ask that a change be made to the proposed rule so that a credit union could request a waiver to the single borrower limit, similar to what is allowed today.

Estimation of Time to Comply

NCUA has asked that credit unions comment on the accuracy of NCUA’s estimates on the burden of the paperwork requirements. The proposal estimates it will take roughly 16 hours

on average for a credit union to update their policies to comply with the proposed rule. We believe this estimate is grossly understated! Although it is difficult to give an accurate estimation of the time that will be needed, we believe it will take hundreds of hours just to update our policies. This doesn't include the numerous hours it will take to read and understand the new rules, evaluate the impact, and educate staff, management, and the Board so they understand their responsibility to comply with the rules. We may also need to research and implement new software to manage the new reporting requirements.

The proposal also estimates that it will take a credit union 160 hours to create the necessary risk rating models. While we understand the importance of a sound risk rating system, it is difficult to understand how it will only take 16 hours to update our policies, but 160 hours to create risk rating models. How complex does the NCUA want the risk rating system to be if it will take 160 hours to create the system? NCUA needs to provide more guidance on exactly what they want in our risk rating models.

Supervisory Guidance

We are concerned that NCUA will provide supervisory guidance for credit unions, in addition to the proposed rules, that will look much like the current requirements. Supervisory guidance does not undergo the public comment period typically associated with the promulgation of a regulation. How extensive would the supervisory guidance be (level of detail and areas covered, for instance)? What would be the degree of enforcement/enforceability of supervisory guidance vs. the published rule?

We are concerned with the guidance that will be provided to examiners. We ask that this guidance be shared with credit unions, allowing an appropriate period for credit unions to review and comment. We also believe it is critical that examiners receive the appropriate training and guidance so our exams will be fair and consistent. This has not always been our experience and with the proposed rules, we fear we will be forced to jump through many hoops, oftentimes burdensome ones, to comply with an individual examiner's personal agenda.

Additional Comments

Compliance has become very difficult, if not impossible, for credit unions over the last decade. The primary reason for this is the ever changing regulations, the letters to credit unions, Office of General Counsel (OGC) letters, and interagency guidance. As long as NCUA is changing the MBL regulations, we would like to see the regulations updated so they are inclusive of all of the MBL/Commercial loan requirements. We do our best to comply, but it is extremely difficult when we have to know hundreds of regulations, in addition to guidance or letters to credit unions that were written many years ago. For example, during our 2014 NCUA examination, the findings referenced NCUA letters to credit unions from 2008 and 2010, and an OGC letter from 2004. How can credit unions possibly be expected to keep up with the regulations, in addition to letters that were written many years ago? We respectfully ask that NCUA make an effort to help credit unions comply with regulations instead of making it more cumbersome.

We are also concerned with how the new rules will be interpreted by examiners. Under the current rule and in the proposed rule it states that a credit union's commercial loan policy must address certain items. In our experience, this has been interpreted to mean different things by different examiners. For example, our policy addressed collections; however, the examiner required us to put our entire collection procedure into policy.

Additionally, the proposed rule requires that we establish a risk rating system. The commentary to the proposed rule states that the procedures and policies outlined in NCUA Accounting Bulletin No. 06, Attachment 1, Loan Review Systems or any updates to this guidance must be reflected in the credit union's policy. We are concerned that this could be interpreted to mean that the entire bulletin, as referenced, must be included in our policy. This is very concerning!

Summary

We thank the NCUA for listening to credit unions and taking steps to improve the current MBL rules. As stated above, we are pleased that the proposed rule will eliminate specific limits within the MBL regulation. We agree with the removal of specific limits in the proposed regulation, including the requirement for personal guarantees, the maximum aggregate unsecured loan limit, and the removal of the loan to value limits.

Credit unions already face many undue regulatory burdens and these burdens take the focus away from serving members by redirecting our focus on responding to regulations. We ask that you consider our comments and suggestions, and make changes to the proposed rule as stated above.

We thank you for the opportunity to comment and for your time and consideration. We encourage you to make the best decision for credit unions and the members they serve.

Respectfully,



Roger R. Heacock
President & CEO

cc: Credit Union Association of the Dakotas
cc: Credit Union National Association